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Office of the Attorney General
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MORTGAGE COMPANIES, ESCROW AGENTS:

Mortgage companies may not act as escrow agents or otherwise control funds which are the subject of completed construction loans. Such funds must be disbursed to an escrow agent independent of the mortgage company, or to the borrower or his designee.

Mr. Burns Baker
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Financial Institutions Division
406 E. Second Street
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Dear Mr. Baker:

As the result of a recent examination, the Financial Institutions Division ("Division") has discovered a practice by some mortgage companies licensed under NRS ch. 645B of maintaining special accounts for the disbursement of loan proceeds used for construction. Although the loan documentation has been completed and security instruments recorded, the mortgage company holds the proceeds and disburses the money in increments to fund the construction for which the loan was made. You have asked the following with respect to this practice:

QUESTION

Is a mortgage company authorized to act as an escrow agent or construction control with respect to the proceeds of a completed construction loan?

ANALYSIS

NRS ch. 645B governs the licensing and regulation of mortgage companies in Nevada. With certain exceptions not applicable here, a mortgage company includes any person who acts as an agent of a lender or borrower

with respect to a loan secured by a lien on real property or who makes such a loan himself. NRS 645B.010(3).

NRS ch. 645A governs the licensing and regulation of independent escrow agents, those who are not employed as escrow officers for title insurers or agents. See NRS 645A.010; 645A.015(1); 692A.128. The provisions of NRS ch. 645A do not apply to "(a)ny firm or corporation which lends money on real or personal property and is subject to licensing, supervision or auditing by an agency of the United States or of this state." NRS 645A.015(3). Because they are subject to licensing, supervision and auditing by the Financial Institutions Division, we believe mortgage companies are exempt from the licensing requirements of NRS ch. 645A.

Since your inquiry relates specifically to the holding of funds for construction, it is necessary to examine the provisions of NRS ch. 627, the Construction Control Law, which imposes bonding and other requirements on persons engaged in the control or disbursement of funds to be used for construction. See NRS 627.050; 627.180; 627.190.

A 'construction control' is any person that engages in the control or disbursement of any funds payable or paid to laborers, materialmen, material suppliers, contractors, subcontractors, architects, engineers or others, for the purpose of satisfying bills incurred in construction, repair, alteration or improvement of any premises or that engages in the processing or approval of any mechanic's lien release, voucher or authorization for payment of a labor bill, or material bill when such bill is incurred in the construction, repair, alteration or improvement of any premises. NRS 627.050.

A mortgage company that disburses loan proceeds in increments to pay bills incurred in the construction to which the loan relates appears to act as a construction control as defined in NRS 627.050. We note, however, that a "lender" under NRS ch. 627 includes "... any person doing business in the State of Nevada, providing moneys to be used in the payment of bills incurred in the construction, repair, alteration or improvement of any premises." NRS 627.100. The Construction Control Law does not apply to "(a) lender of construction loan moneys, provided that he disburses the funds directly to a contractor authorized by the borrower to do the work, or disburses the funds directly to the owner of the premises." NRS 627.210(4). We conclude, therefore, that a mortgage company disbursing construction loan proceeds in increments to the contractor or owner of the premises is exempt from the provisions of NRS ch. 627.

It appears that mortgage companies doing business in Nevada are not prohibited by any provision of chapters 627 or 645A of NRS from maintaining construction control or escrow accounts that disburse funds for construction to the contractor or owner of the premises. The question remains, however, whether the practice is authorized by the license issued under NRS ch. 645B.

A mortgage company license entitles its holder to engage in the activities authorized in NRS ch. 645B. NRS 645B.020(3). NRS 645B.175(1) provides in part:

1. All money received by a mortgage company from a person to acquire ownership or a beneficial interest in a loan secured by a lien on real property, must;

(a) Be deposited in:

(1) An insured depository financial institution; or

(2) An escrow account which is controlled by a person who is independent of the parties and subject to instructions regarding the account which are approved by the parties.

Funds held in trust pursuant to this section must be released:

(a) Upon completion of the loan, including proper recordation of the respective interests or release, or upon completion of the transfer of the ownership or beneficial interest therein, to the debtor or his designee less that amount due the mortgage company for the payment of any fee or service charge;

(b) If the loan or the transfer thereof is not consummated, to the person who furnished the money held in trust; or

(c) Pursuant to any instructions regarding the escrow account.

NRS 645B.175(2). Subsections 3 and 4 of this statute impose similar requirements on the handling of funds paid to the mortgage company in payment of the loan. Licensees must submit to the commissioner of the Division ("commissioner") an audited financial statement within 60 days after the close of their latest fiscal year if they maintain any accounts described in NRS 645B.175(1). NRS 645B.050(2) and (3).

We note that your question does not concern the practice of a mortgage company holding funds pending the completion, or closing, of the loan itself. We believe that NRS 645B.175(1)(a)(1), authorizing the company to deposit funds to be used in making loans in an insured depository financial institution until the completion or transfer of the loan as described in subsection (2)(a) of that statute, permits a mortgage company to hold funds not yet subject to a particular, completed loan, subject to the time limitation described in subsection (6) of the statute. Alternatively, the company may deposit such funds directly into "(a)n escrow account which is controlled by a person who is independent of the parties and subject to instructions regarding the account which are approved by the parties." NRS 645B.175(1)(a)(2).

Upon completion of the loan, however, the mortgage company's obligation changes. At that point, the funds must be "released ... to the debtor or his designee ..." or "(p)ursuant to any instructions regarding the escrow account." NRS 645B.175(2)(a) and (c). We believe that the escrow account described in subsection (2)(C) refers to the escrow account into which funds were initially deposited pursuant to subsection (a)(1) and (2) of the statute. These two sections, when read together, authorize the loan proceeds to be released pursuant to escrow instructions only if they were initially deposited into an escrow account established pursuant to subsection (1)(a)(2) of NRS 645B.175. If the funds were initially held by the mortgage company in an insured depository financial institution pursuant to subsection 1(a)(1) of the statute, they must be released upon completion or transfer of the loan "to the debtor or his designee." NRS 645B.175(2)(a).

Although we believe this conclusion is compelled by the plain language of the statute, it does not end our inquiry. The question remains whether the mortgage company may be considered "a person who is independent of the parties" as described in NRS 645B.175(1)(a)(2). If so, the company may act as escrow agent and control the disbursement of funds in the account described in that section "subject to instructions regarding the account which are approved by the parties." In addition, the question arises whether a mortgage company may properly be deemed a designee of the borrower under NRS 645B.175(2)(a) authorized to hold funds on the borrower's behalf after completion of the loan. To resolve these issues, we refer to several accepted rules of statutory construction.

The leading rule of statutory construction is to ascertain the intent of the legislature in enacting the statute. *McKay v. Bd. of Supervisors*, 102 Nev. 644, 650, 730 P.2d 438 (1986). Where a statute is clear on its face, a court may not go beyond the language of the statute in determining the

legislature's intent. *Thompson v. District Court*, 100 Nev. 352, 354, 683 P.2d 17, 19 (1984). Where a statute is capable of being understood in two or more senses by reasonably informed persons, it is ambiguous and should be construed "in line with what reason and public policy would indicate the legislature intended." *Robert E. v. Justice Court*, 99 Nev. 443, 445, 664 P.2d 957 (1983).

Where a statute is ambiguous, the meaning of the words used may be determined by examining the context and the spirit of the law or the causes which induced the legislature to enact it. *McKay*, supra, 102 Nev. at 650-651. The entire subject matter and policy of the law may be involved as an interpretive aid. *Id.* Words in a statute having a well-defined meaning at common law are presumed to be used in their common law sense, unless it clearly appears that another meaning was intended. *Moser v. State*, 91 Nev. 809, 544 P.2d 424 (1975). Statutes should always be construed to avoid an absurd result. *State v. Webster*, 102 Nev. 450, 726 P.2d 831 (1986).

Applying these rules to the question posed, we conclude that a mortgage company may not properly be viewed as "a person who is independent of the parties" as required by NRS 645B.175(1)(a)(2). In those situations where the mortgage company acts as the lender, it could not, by the plain language of the statute, be considered "independent of the parties." Where the mortgage company acts only as the agent of the lender or borrower, it is also not independent. At common law, an escrow did not exist if the object purportedly held in escrow was delivered to an agent of the intended recipient. See *State, By Pai v. Thom*, 563 P.2d 982, 987 (Haw.1977); see also, Nev.Op.Att'y Gen. No. 84 (October 24, 1963). We can discern no intent to change this aspect of the common law definition of escrow. We conclude, therefore, that a mortgage company may not control the escrow account described in NRS 645B.175(1)(a)(2) and (2)(c). If funds received by a mortgage company are to be deposited into escrow pursuant to this statute, the account must be controlled by an escrow agent who is independent of the mortgage company whether it is a direct party to the loan or an agent of one of the parties.

We also conclude that a mortgage company may not act as the debtor's designated recipient of the loan proceeds under subsection (2)(a) of NRS 645B.175. Such an interpretation may be permitted by the literal language of the statute; however, we believe it produces an absurd result not intended by the legislature.

The legislature intended to limit the circumstances under which mortgage companies may hold money belonging to others and to require strict

accountability for money so held. Money held for making loans must be kept separate from money belonging to the mortgage company and money received in payment of loans. NRS 645B.175(1)(b). Money received for the payment of taxes and insurance on property securing loans made by the company must be kept separate from all other funds held by the company. NRS 645B.170; 645B.180. Where the legislature intended to authorize a mortgage company to hold money belonging to others, it did so expressly and included a requirement that the company be fully accountable to the commissioner for the money so held.

The legislature in NRS 645B.175(1) and (2) specifically limited the circumstances under which a mortgage company may hold funds received for making loans in a non-escrow trust account to the time pending completion or transfer of the loan. Moreover, funds may be held in that status for no more than 45 days. If, within this period, the loan is not consummated or an escrow account opened in connection with the loan, the money must be returned to the investor within 24 hours. NRS 645B.175(6). Funds so held must be reflected in an annual, audited financial statement, a copy of which is submitted to the commissioner at the same time it is delivered to the company. NRS 645B.050(2)(3).

We conclude that by specifically limiting the circumstances under which a mortgage company may hold funds received for making loans in a non-escrow trust account to the time pending completion of the loan, and by establishing strict accounting procedures with respect to money so held, the legislature intended to prohibit a mortgage company from controlling the funds after completion of the loan. Had the legislature intended to authorize a mortgage company to maintain a special account for the disbursal of a completed construction loan, an account not subject to the strict accounting procedures established for other types of accounts regulated by the statute, it would have done so expressly.

CONCLUSION

Although not prohibited by any provision of the Independent Escrow Agent's Act, NRS ch. 645A, or the Construction Control Law, NRS ch. 627, from maintaining a construction control or escrow account to disburse the funds of a completed construction loan, mortgage companies may not engage in such activity unless it is authorized by the mortgage company license issued to them under NRS ch. 645B. Pursuant to NRS 645B.175(1) and (2), mortgage companies may not act as escrow agents or otherwise control funds which are the subject of completed construction loans. If the proceeds of completed loans are disbursed pursuant to escrow instructions,

the escrow must be administered by an escrow agent who is independent of the mortgage company. In addition, a mortgage company may not control such funds by being designated as the recipient of the loan proceeds by the debtor, as such an interpretation would defeat the legislature's intent to limit the circumstances under which a mortgage company may hold funds belonging to others and to require strict accountability as to funds so held.

Very truly yours,

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